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May 9, 1997

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The Honorable John D. Dingell
Ranking Member
Commerce Committee Democratic Office
564 Ford House Office Building
U.S. House of Representatives
Washington, DC 20515

Dear Congressman Dingell:

Thank you for your letter of April 10, 1997 and this opportunity to submit our views concerning legislation affecting the electricity industry. I will attempt to answer, in turn, each of the questions set forth in your April 10th letter, although there will be considerable overlap in certain areas.

Query 1. *From your company's point of view, is it necessary for Congress to enact legislation bearing on retail competition, and why? If you favor legislation, please outline which issues should be addressed and how you think they should be resolved.*

Response. GPU believes Federal legislation is necessary to insure full and fair retail competition in the electric power industry. While states are exercising their authority to implement retail choice, Congress must act to ensure the creation of a nation-wide equitable and fully competitive retail electricity market

GPU recommends that Congress seek to achieve four goals in restructuring legislation.

I. Ensure Recovery of Transition Costs

GPU strongly supports the introduction of meaningful retail competition provided that it is implemented fairly and with appropriate protection for prudently incurred investments and commitments. To this end, Federal restructuring legislation must ensure that a reasonable opportunity is provided for full recovery of these costs, particularly those costs resulting from federal mandates.

II. Remove Federal Barriers to Competition.

□ *Repeal the Public Utility Holding Company Act of 1935 (PUHCA):* Both of the states served by GPU's domestic utility affiliates (Pennsylvania and New Jersey) are implementing full retail choice. However, as regulators and participants in this new market prepare for the onset of full competition, registered holding companies remain competitively disadvantaged by PUHCA's outdated and unnecessary restrictions. PUHCA also creates needless barriers to the entry of new competitors into the market. Therefore, Congress should act immediately to repeal PUHCA to ensure that customers receive the benefits of a fully competitive electricity market.

□ *Reform the Public Utility Regulatory Policies Act (PURPA):* PURPA's anti-competitive special privileges provided to certain qualifying generators will remain in place *after* full competition is implemented in Pennsylvania and New Jersey unless Congress acts. PURPA contracts are responsible for an estimated one-quarter of the electric industry's above-market costs, according to a recent study by Resources Data International. Congress should act now to repeal PURPA's mandatory purchase obligation to ensure that this law does not continue to impose unnecessary costs on consumers during and after the transition to retail competition. As noted above, Congress must ensure that costs mandated under PURPA are recovered.

III. Preserve State Customer Choice Laws

While Congress must enact legislation to ensure the creation of a nation-wide equitable and fully competitive retail electricity market, the states should be allowed to determine the pace and shape of the transition to full customer choice. Federal restructuring legislation should preserve the states' freedom to develop appropriate mechanisms, guidelines and protocols which are best suited to encourage and enhance competition in light of each state's particular circumstances. Existing state retail choice plans should be grandfathered.

IV. Level the Competitive Playing Field

□ *Eliminate Subsidies for Public Power:* Public power entities now exempt from the Federal Energy Regulatory Commission's (FERC) Orders 888 and 889 should be legislatively subjected to FERC's open wholesale access rules. In addition, competitively neutral new rules for both private and public utilities must be adopted to create efficient regional and national retail markets.

□ *Provide a Nationwide Market for Retail Sales :* Congress should either mandate retail customer choice by a date certain or otherwise ensure freedom to sell at retail across state lines.

□ *Define State and Federal Regulatory Jurisdictions:* The line between Federal and state regulatory jurisdictions needs to be clearly defined.

Query 2. *If the state(s) you serve has adopted or is considering adopting retail competition, what are your biggest concerns? Please be specific. Indicate how you are dealing with them and any recommendations you may have.*

Response. In the two states in which GPU's domestic utility affiliates operate, New Jersey and Pennsylvania, the restructuring efforts are well advanced. In New Jersey, the

Board of Public Utilities (BPU) recently released its Energy and Master Plan II setting forth its Findings and Recommendations for the Restructuring of the Electric Power Industry. The BPU has recommended to the Governor and the Legislature that retail competition be introduced in New Jersey in phases, commencing in October 1998, with all customers to be able to select their electricity suppliers by 2000. In Pennsylvania, the Electricity Generation Customer Choice and Competition Act, which was enacted in 1996, also provides for a phase-in of electric competition beginning on January 1, 1999 with choice for all customers by January 1, 2001. Restructuring filings with the relevant state commissions are due in both states over the next few months.

Our primary concern regarding the implementation of the respective state retail competition plans is to retain respect for the significant commitments previously made by utilities for prudent investments in utility plant for the benefit of their customers, as well as commitments relating to power purchase agreements with non-utility generators which were entered into under the auspices of PURPA. Such investments and commitments were mandated and/or sanctioned by various governmental structures and were recoverable under the prevailing regulated environment when made, but are likely to become uneconomic to some degree in the new competitive environment. Both New Jersey and Pennsylvania appear to have made appropriate provisions for addressing these concerns, although it will be necessary to monitor the numerous company-specific proceedings in each state to insure that such principles are properly implemented. As discussed above, we believe that federal legislation providing for recovery of these stranded costs, particularly those cost created by government mandates under PURPA, are critical to the Federal restructuring legislation.

A second concern with the transition from a regulated monopoly to a market-based competitive industry, is the timely creation of orderly processes which enhance the attainment of the goal of providing safe, adequate, reliable and reasonably priced electricity. Given the number of pivotal issues to be addressed, it is critical that the schedule permit sufficient time for preparation of comprehensive and accurate proposals by the utilities, and for their review by the state regulators. Utilities and regulators must be allowed enough time to review, evaluate, modify if necessary, and implement retail competition while maintaining and improving on the level of access to reliable and reasonably priced electricity in a marketplace which protects and enhances competition on the merits without imposing or creating artificial competitive advantages for some competitors and disadvantages for others.

Query 3. *Whether or not you favor federal legislation, please indicate your position on the following specific issues (to the extent not addressed in your responses).*

a. A Federal mandate requiring states to adopt retail competition by a date certain. If retail competition is under consideration in the state(s) you serve, do you believe Congress should provide additional direction or authority?

Response. Imposition of a federally mandated specific date certain for the implementation of retail competition is not critical. In Pennsylvania and New Jersey, we see reasoned approaches to the phase in of customer choice that seem to give due consideration to operational and reliability concerns. What is critical, however, is the substance and details of any Federal electricity legislation. For instance, an early date for implementing customer choice in a well-drafted bill which repeals Federal barriers and enhances or increases the likelihood of a level competitive playing field would be beneficial. However, a bill having a later date for retail competition that added confusion or delay to the restructuring process, gave artificial preferences to some competitors or maintained unnecessary burdens on others would be detrimental to the creation of an efficient retail electricity market.

b. Recovery of stranded investment. If the state(s) you serve already has adopted retail competition, how was this issue addressed and are you satisfied with the outcome? If your state(s) is considering adopting retail competition, how would you recommend that this issue be treated? Do you think Congress should enact legislation relating to stranded cost issues, and if so what would you recommend? Is securitization a useful mechanism for dealing with stranded costs, and whom does it benefit?

Response. It is our understanding that most of the approximately 10 states which have adopted retail choice plans over the last year have also provided for full recovery of stranded costs. Two states - Arizona and New Hampshire - not allowing for such full recovery are now embroiled in attempting to resolve disputes and litigation flowing from that decision . On the federal level, FERC has also provided for full recovery of wholesale stranded costs in its Order 888 providing for open access.

As discussed previously, Pennsylvania and New Jersey have taken significant steps to implement retail competition. Pennsylvania has adopted the Pennsylvania Electricity Generation Customer Choice and Competition Act which provides for retail choice to be made available to all customers by 2001. In New Jersey, the BPU has proposed a plan to implement retail competition in a time frame similar to Pennsylvania.

Both states have provided or are proposing to provide for full recovery of stranded costs (those reasonable and prudent investments and commitments made by utilities in the past, under the service obligations and restricted investment returns allowed by traditional regulation, which should be honored in and through the restructuring process), including generation-related investments and commitments, such as nuclear decommissioning costs, above-market power purchase agreements with non-utility generators and certain regulatory assets. In Pennsylvania, the mechanisms for recovery of stranded costs include a non-bypassable transition charge to customers, securitization and, in some instances, limited exceptions to a rate cap which would otherwise apply during the transition to competition.

Securitization of stranded costs, which is specifically authorized by the Pennsylvania restructuring legislation and contemplated by the New Jersey BPU's Findings and

Recommendations, is a significant tool for protecting the legitimate interests of existing utility investors to obtain an appropriate return of and on their investments, while at the same time allowing for prompt rate reductions to customers as a result of the lower financing costs of the securization. Indeed, without securization, some of the benefits of competition may be delayed or forestalled.

With respect to stranded costs, we would support Congressional action which:

- Links the utility's duty to grant open access to all of its transmission and distribution facilities with a corresponding duty on FERC and state regulators to give the utility a reasonable opportunity to fully recover all legitimate and verifiable wholesale and retail stranded costs, including full recovery of stranded PURPA costs, over a time period and in a manner which does not adversely affect the utility's financial integrity.

- Uses non-bypassable distribution and transmission charges, service or access charges, or exit fees, to effect any recovery. These fees and charges should not unduly discriminate among different customer classes, nor shift cost responsibility among different classes.

- Prevents new determinations of stranded costs and their allocation among different customer classes (or among the different states served by multi-state utilities), thereby preventing conflicts with or rejections of earlier state prudence determinations or FERC cost allocations for multi-state power projects.

- Allows for federal preemption of states which fail to comply with these requirements allowing for the imposition of properly-calculated retail transition cost surcharges or exit fees on local distribution services or customers.

c. *Reciprocity. Can states condition access to their retail markets on the adoption of retail competition by other states? Should Congress enact such a requirement? Could such a requirement create an incentive for states with low electric rates not to adopt retail competition, in order to keep cheap power at home?*

Response. GPU believes that regional cooperation among the states is necessary to realize the full potential of competition. Regional cooperation is indispensable to maintain system reliability.

Such cooperation, however, requires that all of the participants be operating on a level playing field. For example, in an attempt to level the playing field, the Pennsylvania law includes a reciprocity provision. Specifically, the provision allows for two six-month delays in the transition period if Pennsylvania generators are disadvantaged due to the lack of regional reciprocity and where the interests of Pennsylvania business and industry would be materially affected. There is concern that generators from states other than Pennsylvania will compete against Pennsylvania companies while the Pennsylvania based companies are not afforded similar opportunities beyond their state's borders. Federal legislation should otherwise address the issue of establishing a national retail energy market, if there is no federal mandate for retail customer choice by a date certain.

Query 4. *If Congress enacts comprehensive restructuring legislation, should it mandate "unbundling" of local distribution company services? What impact would this have, and would the effects differ for various customer classes? Would this entail substantial expense, and who would incur any such costs?*

Response. We do not support Congressional action to mandate *"unbundling" of local distribution company services* for the following reasons:

The subject of local distribution "unbundling" entails two distinct types of unbundling.

The first type of "unbundling" entails the separation of the generation (i.e., power supply) charges from the delivery charges relating to use of the utility's distribution network. Such "unbundling" is designed to create a more transparent market that will, among other things, allow customers to readily compare energy prices. This aspect of "unbundling" is being adequately and appropriately addressed at the state level. Indeed, as part of the various state proceedings, including in New Jersey and Pennsylvania, "unbundling" of these various charges is being specifically addressed in the context of each state's particular circumstances, with due regard for the impacts on the various customer classes.

The other type of "unbundling" relates to the definition of "local distribution company services", which could see the concepts of "open access" and "customer choice" extended beyond the selection of unbundled energy suppliers to encompass other "services" such as billing, metering, energy management services and equipment sales. Customer choice in these areas is not central to the creation of a competitive generation market, which is the underlying goal of industry restructuring, and competition in some or all of these areas may not make economic or operational sense in any event. Indeed, most participants in the restructuring debate assume that transmission and distribution will remain regulated activities, at least for the foreseeable future. Existing regulatory authority is adequate to deal with the provision of the above-described services. As a result, Congress should leave to the states decisions as to the possible "unbundling" of these services because they are more familiar with the local circumstances affecting such decisions.

Query 5. *Recently Chair Moler of the Federal Energy Regulatory Commission recommended that, as part of comprehensive legislation, Congress authorize the Commission to enforce compliance with North American Electric Reliability Council standards to help maintain reliability of service. Do you believe this is necessary, and why or why not?*

Response. We agree with and support Chair Moler's proposal. In light of the central significance of electricity supply to the economy and to the health and safety of the citizenry we believe that FERC should be given back-up authority to enforce compliance with relevant reliability standards. We support the Chair's proposal even though, in our view, the North American Electric Reliability Council (NERC) and the other regional reliability councils have historically been effective in formulating necessary reliability criteria and protocols. In this regard we also note that NERC and the regional councils are evolving in the transition to competition and that the states are expected to require all electricity suppliers to join, or conform to the requirements of, such councils. In addition, NERC and the regional councils have modified their by-laws to require compliance with relevant criteria and protocols. However, the significance of reliability issues and concerns on balance weigh in favor of Federal regulatory enforcement authority once NERC and regional council sanctions have failed.

Query 6. *What concerns does your company have with respect to the role of public power and federal power marketing agencies in an increasingly competitive wholesale electric market? In markets in which retail competition has been adopted? Are there concerns you would like to have addressed if Congress enacts comprehensive restructuring legislation? Should Congress consider changes to federal law as it applies to regulation of public or federal power's transmission obligations?*

Response. In our view, all participants in the new competitive marketplace must compete on an equal footing. This will require, among other things, that there be regulatory and financial parity between public and private power. Indeed, the tax and other public subsidies inherent in public power and federal power marketing agencies have long since fulfilled their intended purposes, and are no longer needed. To create a truly competitive market and properly reward the efficient producers, all energy suppliers must live by the same business and regulatory standards and must be prevented from selling power in a competitive market at artificially low (i.e., subsidized or otherwise not economically or cost justified) prices or from benefiting from preferential tax treatment. The restructured electricity industry can no longer support tax exempt financing by public power or its access to subsidized government power for resale in competitive markets. Congress should eliminate these inherently unfair and anti-competitive subsidies. In addition, the open access requirements of FERC Orders 888 and 889 must be applied to all public power entities.

Query 7. *If Congress enacts comprehensive restructuring legislation, should changes be made to federal, state or local tax codes, and if so why? Please be specific.*

Response. Yes. Federal, state and local tax laws will have to be adapted to provide for a level playing field for all electricity suppliers, whether utilities or non-utilities. Put simply, fundamental differences of historic tax treatment, including those related to public power mentioned above, should not be allowed to create or destroy the competitive position of any participant in the future energy marketplace. .

It may be useful to note that the New Jersey Legislature, at the behest of the BPU, is considering comprehensive state tax reform legislation which would level the playing field by subjecting all suppliers to the same state taxes, while protecting against sharp declines in revenue streams through a transitional tax. The Pennsylvania restructuring law also addresses the need for tax parity by requiring all licensed energy suppliers to pay taxes equivalent to those imposed on regulated utilities, preventing tax shifting among customer classes and seeking to preserve the overall level of tax revenues traditionally generated by electricity services.

Query 8. *What, if any, concerns do you have about the reliability of the electric system? If the industry moved to retail competition, will adequate reserves be available? Is the transmission system capable of handling full retail competition?*

Response. In the near term, the existing oversupply of generation should insure adequate supplies of electricity. In the longer term, we believe that system reliability and adequate generation reserves can and will be maintained in a competitive market responding to appropriate pricing signals, supported by the mandatory standards of NERC and the regional electric reliability councils and the "back-up" enforcement authority to be vested in FERC.

While existing physical transmission constraints may impede some market transactions that might otherwise occur in the absence of such constraints, we believe that the marketplace itself will set the threshold values at which such constraints will be removed through market forces, if pricing is fair and it is economically appropriate to do so. Those constraints having a reliability impact will be resolved through action of the electric reliability councils (or ultimately FERC) if the market fails to do so.

In this regard, we note that the FERC proceedings in connection with the restructuring of the PJM Interconnection, including the FERC technical conference on transmission pricing to be held on May 9, are indications that the complex and sensitive issues related to transmission pricing are being addressed. We are hopeful that those proceedings will result in reasonable resolution of these issues in line with the positions proposed by the PJM Supporting Companies in those proceedings.

We also note that both New Jersey and Pennsylvania will be addressing reliability concerns in their restructuring proceedings, intending to impose reliability burdens on all suppliers proportionately, not just the regulated utilities.

Query 9. *If Congress enacts legislation on retail competition, should* *changes to the Public Utility Company Holding Company Act of 1935 (PUHCA) be included? If so, what would you recommend? In particular, how should Congress address market power concerns in any such legislation? Are transition rules needed during the period before effective competition becomes a reality?*

Response. As mentioned earlier, PUHCA is a costly anachronism which prevents the registered holding company systems from competing on an equal footing with other utilities. Therefore, PUHCA should be repealed as soon as possible, and should not await retail competition legislation. Indeed, the Securities Exchange Commission (SEC) and the National Association of Regulatory Utility Commissioners have stated that PUHCA is no longer necessary to regulate utility holding companies. Nonetheless, PUHCA's regulatory requirements continue to impose substantial costs on registered companies. Repeal of PUHCA would facilitate competition by the registered holding company systems and others (by removing barriers to entry) whether retail competition occurs quickly or is phased in.

There is no need for Congress to address market power concerns in PUHCA repeal legislation. Any market power issues are not peculiar to holding companies and should be addressed generally. The integrity of the market has been, and will continue to be, protected by the Department of Justice under the federal antitrust laws, and through FERC and state regulation of terms and conditions of service.

Because PUHCA repeal would have no anti-competitive effect, no transition rules are required during the period of implementation of retail competition.

Query 10. *To what degree, if any, have recent Securities and Exchange Commission administrative orders and Rule 58 decreased the need for legislative changes to PUHCA? Assuming these actions withstand any court challenges, what are your major remaining concerns about the Act?*

Response. We support the SEC's recent administrative orders and Rule 58. Any effort to rationalize the regulatory regime and to reduce unwarranted federal regulatory burdens enhances competition and benefits our customers and shareholders.

Rule 58 and other administrative orders are not, however, a substitute for PUHCA repeal. Although the SEC can, by administrative action, decrease somewhat the number of transactions for which registered companies require prior approval from the SEC, and increase somewhat the registered companies' ability to take the same steps that are available to exempt and stand-alone companies today, the registered companies continue to be subject to significant limitations not imposed on other participants in the utility sector or on any other industry competing for financing and investors.

For example, registered companies continue to require prior SEC authorization to enter into many service, sales or construction contracts with affiliated companies; and continue to be subject to SEC regulation of certain intrasystem and other financial transactions.

The SEC has recognized that PUHCA is no longer required. Nonetheless, many of its anti-competitive restrictions remain in place, and Rule 58 and other administrative reforms of PUHCA remain subject to rescission or reinterpretation. Without repeal, the registered companies will continue to be restricted by unnecessary limitations on their ability to compete, the costs of which are borne by their customers and shareholders.

Query 11. *As electricity markets have become more competitive, some have asserted that PUHCA prevents consumers from receiving the full benefits of competition. Do you agree or disagree, and why? Is competition in wholesale or retail electric markets dependent upon the participation of the registered holding companies? Is it a certainty that changes to PUHCA would enhance actual competition? Please provide specific examples to illustrate your answers.*

Response. GPU agrees that PUHCA bars consumers from receiving the full benefits of competition because costs and limitations on any company owning 10% or more of a public utility company, by imposing PUHCA severely limits the number of companies willing to enter electric power markets. Such restrictions on the entry of new competitors retards the creation of a more active and robust market, decreases competition and increases the cost of power paid by consumers.

In order to avoid PUHCA, new entrants are limited to two specific modes of competition - Qualified Facilities and Exempt Wholesale Generators, both of which were made available only by amendments to PUHCA and the Federal Power Act. Other efficient modes of competition are still closed to those who see great disadvantages in registering under PUHCA.

Thus, even with competition, these additional costs PUHCA imposes on registered companies will keep the price paid by consumers artificially high, either through the higher prices that must be charged for the registered companies' power or through the artificial restrictions which hinder potential competitors from entering relevant markets, with such restricted markets commanding higher prices than would otherwise prevail. By repealing PUHCA, Congress can lower prices and boost competition.

Query 12. *Do registered holding companies face unique problems if some states they serve adopt retail competition and some do not?*

Response. We do not believe that the registered holding company systems are unique in the context of assessing the impact of differing approaches to the implementation of retail competition by the states. In particular, we do not anticipate any particular problems affecting our holding company system as a result of inconsistent or contradictory actions at the state level. Indeed, the actions taken so far in New Jersey and Pennsylvania, where the GPU domestic utilities operate, do not raise any such concerns.

Query 13. *How do the various retail competition proposals presently pending before the Congress affect decisions regarding stranded costs for registered holding companies? Do you support any of the formulations in these bills? Do you have alternate recommendations on this or other issues unique to registered holding companies if Congress enacts retail competition legislation?*

Response. Except for the necessity to repeal PUHCA, pending legislation would not affect registered holding companies differently from other utilities. To the extent that such proposals require the recovery of prudently incurred stranded costs, they would not affect decisions in this area for registered holding companies.

Very truly yours,

F.D. Hafer

F.D. Hafer,
President & Chief Operating Officer